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SUBJECT: NON-DOM TAX ISSUE HEATS UP

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¶1. This cable contains an action request. See paras 8 and 9.

¶2. (SBU) Summary and Action Request: The proposed taxation of non-domiciled foreigners in the UK (including Americans) continues to roil the business world here. Trade and Investment Minister Lord Digby Jones warned against implementing the proposed changes to the tax rules on the front page of the February 8 Financial Times (FT). David Lewis, Lord Mayor of London, also chimed in against the change as has the head of the American business association. On February 12, Chancellor Darling, responding to public pressure, slightly modified the government's proposal, to allay fears that UK tax inspectors would probe into foreign assets, but without addressing the main concerns of U.S. taxpayers. Resident Americans worry that, although the final legislation will not be approved by Parliament until summer 2008, the law will be effective as of April. This means that the U.S. Department of Treasury will not be able to determine if the new taxes are creditable against U.S. taxes until after the law is already in effect. An HM Treasury (HMT) official will be in Washington the week of Feb 19 to discuss this issue, among others. They have signaled their willingness to dialogue with U.S. counterparts about what might or might not be creditable. ACTION REQUEST: There are many competing U.S. interests entangled in this topic. We welcome the prompt consultations between U.S. and UK Treasury officials. Meanwhile, post seeks clearance of talking points in paragraph 9. U.S. Department of Treasury Assistant Secretary Swagel and Deputy Secretary Kimmitt should be prepared to

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answer questions on the non-dom issue when they visit London in February and March respectively. (End Summary and Action Request)

Background

¶3. (SBU) HMG intends to require non-domiciled residents of the UK, who have lived in the country seven of the last ten years, to either pay UK tax on their worldwide income, or a flat 30,000 GBP ($60,000) per person charge. Currently, non-domiciled residents only have to pay tax on their domestically earned income and whatever monies they remit to the UK. Domicile is unique British concept: determined by one's father's place of domicile and a theoretical intention to one day depart the UK. It is not related to nationality. The changes will take effect in April. The American business community, represented by British American Business, has opposed these changes since their announcement in the October 2007 pre-budget report, (Reftel B).

Front Page News

¶4. (SBU) In a February 8 Financial Times interview that attracted considerable attention, Trade And Investment Minister, Lord Digby Jones, said that the proposed non-dom tax changes make it harder for him to sell Britain as a destination for skilled foreign workers and inward investment,. Jones said that many individuals from the financial industry had told him this is a serious issue for the industry. Jones said he had not been consulted on the change before it was introduced in October's pre-budget report. David Lewis, Lord Mayor of London, has also weighed in. He told the Chancellor he found real anxieties over the proposed changes in many meetings with the financial industry. The front page of the Financial Times ran another story on February 11 with the misleading headline "U.S. in tax clash with UK over non-doms." The article contained a quote we supplied noting that the Embassy was passing concerns it had heard to HMT. The Times also issued an editorial which strongly opposed the non-dom tax change. In addition, Bloomberg, Forbes and the BBC have contacted us seeking comment.

Some Adjustments

¶5. (SBU) To damp down the media frenzy, on February 12, Chancellor of the Exchequer Darling announced slight modifications to the proposal, without addressing the core concerns of the U.S. community. Darling said anyone paying the flat GBP 30,000 levy 'will not be required to make any additional disclosures about their income and gains arising abroad' and the changes to the taxation of trusts will not apply to gains before April 6. Also, money brought into the UK to pay the GBP 30,000 levy will not itself be taxable, nor would art works brought in for public display.

But Continuing Concerns

¶6. (SBU) These changes will help quiet some of the more alarmist news stories in the UK (although they immediately gave rise to another set of stories about the Labour government's dithering.)

They do not however address the chief concerns of American residents: double taxation and timing. As currently structured, the UK proposals would probably not meet a U.S. legal definition of an "income tax" and so payments would not be creditable under the U.S.-UK Double Tax Convention. To our knowledge, Americans are only major community in the UK that also has to pay taxes to their home country.

¶7. (SBU) The other major concern among expatriates in the UK, including Americans, is the timing of the proposed changes. In the draft legislation, the law would take effect in April 2008, the beginning of the UK's financial year. However, the final legislation will not be passed until late summer. U.S. Treasury officials are naturally reluctant to voice an opinion on creditability until the final legislation has been thoroughly analyzed. Post is concerned, however, that many American residents of the UK will be unable to properly adjust their financial affairs to account for the changes, because they will have incomplete information at the beginning of the tax year. British American Business (BAB), Germany Industry UK, and many other organizations have requested that if HM Treasury implements this law, it should at least give expatriates adequate time to prepare their financial affairs. The head of BAB, Peter Hunt, told the press February 11 "We don't believe that it is the Government's objective... to reduce the attractiveness of investment in the UK to its largest inward investor. Yet this is likely to be precisely the outcome .... We shall be less likely to attract the current high levels of U.S. investment to the UK. We shall reduce the attractiveness of the UK both to U.S. companies sending staff to the UK, and establishing headquarters operations here where such operations require long-term senior management assignments."

¶8. (SBU) This is a multi-faceted issue with competing interests. Business people, academics and others highlight the advantages of maintaining the current high numbers of Americans in the UK, which

they say facilitate trade, investment and much more between the two countries. The large number of Americans in the UK is also an integral part of the special relationship between the two countries and of our 'soft power'. Another side of the story is the importance of maximizing tax income to the U.S. government, which would militate against crediting the UK charges against U.S. taxes.

Plans for Consultations

¶9. (SBU) Steven Effingham, the lead on this issue at HMT, told us his supervisor, Mike Williams, will travel to Washington the week of February 19 to discuss this and other issues with counterparts at U.S. Treasury. Effingham insists that HMT is willing to consider altering the legislation in order to avoid double taxation of Americans. He has also volunteered to speak at a town hall meeting, where he can answer questions raised by American residents.

Seeking Guidance

¶10. (SBU) HMG, American citizens, tax experts, and the press are coming to the Embassy with questions in increasing numbers. We are not in a position to answer those queries and thus welcome the news that our respective Treasury experts to meet. The issues being raised with us include:

---How likely is it that this tax will be creditable against U.S. tax liability?
Option A: Will the 30,000 GBP ($60,000) charge be creditable?
Option B: If Americans choose instead to declare their worldwide income to the UK, would taxes paid here be creditable?

--- What is the result of U.S. Government engagement with HMT on the issue of creditability?

--- If Americans choose to make their place of domicile the UK, would they then find relief from double taxation under the existing double taxation convention?

Requesting Clearance

¶11. (SBU) Post also requests clearance of the following talking points for use with HMG.

--- The U.S. government respects the right of the United Kingdom to tax its citizens and residents in any manner it sees fit. Many long-term, resident American citizens however have expressed concerns to us about the proposed timeline for implementation of changes to the tax code for non-domiciled residents.

---The U.S. government supports its citizens' requests that they be given a reasonable amount of time between the publication of the

final legislation and the implementation of the law in order to arrange their financial affairs to suit the new tax rules.

---A reasonable waiting period between the publication of the final legislation and its implementation would also give the U.S. Treasury time to analyze the changes fully and determine the creditability against U.S. taxes of any new UK tax charges.

-- We are prepared to work with you discuss what kind of tax would be deemed income tax consistent with the spirit of the U.S. UK Double Taxation Convention, to mitigate adverse consequences on U.S. citizens.

¶12. (SBU) Time is short. If we are to advise American citizens of their likely tax exposure, they need to hear from us sufficiently before April 1 to make arrangements. Also, U.S. Treasury Deputy Secretary Kimmitt and Assistant Secretary Swagel are planning trips

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to the UK within the next month. They are very likely to receive

these same questions.

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